Enhanced Engagement In Fragile States
Revised Approach

Discussion paper

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ENHANCED ENGAGEMENT IN FRAGILE STATES
REVISED APPROACH

PURPOSE & SUMMARY

This paper presents key elements of a proposed revised framework to deepen the Bank's engagement in regional country circumstances that have come broadly to be characterized as fragile. It has benefited substantially from guidance provided on earlier drafts by the Board of Directors and the ADF Deputies.

The case for a major new initiative to support enhanced ADB engagement in fragile states is clear. Numerous African countries are in difficult fragile situations, spanning conditions of marked deterioration, conflict and crisis, post-conflict, transition from crisis, and gradual improvement. Circumstances differ from country to country, and a differentiated approach is needed. A number of countries in particular have emerged from debilitating crisis that has severely degraded living standards and physical and institutional capacity, and imposed wider regional disruptions. For these, a rapid transition to renewed growth and development is urgently needed to strengthen the foundation for stability and progress, both domestically and regionally. But despite a unique set of requirements and opportunities, and the clear need for deeper and more effective international engagement, current mechanisms have thus far proven insufficient. There is wide demand and support for the African Development Bank to take on the major role that it is now better positioned to play.

The Bank' is proposing a revised framework to define this role and to meet specific priorities and expectations expressed by member countries. It provides avenues through which the Bank can be more effectively engaged in countries in all fragile situations, while focusing particularly on a smaller subset of post-crisis/transition situations. In these cases the objective is to set out a limited number of characteristics or criteria to identify individual countries in which enhanced engagement is both necessary and appropriate; develop a mechanism to provide supplementary resources in these cases, scaled to needs, on appropriate terms and a predictable basis; ensure effective performance monitoring and exit criteria; and, modify selected procedures to improve the Bank's own delivery and supervision capacity.

Specifically, the revised framework proposes the following:

1. A supplementary financing mechanism to provide incremental resources for enhanced Bank engagement in post-crisis/transition situations. Eligibility criteria, a specific allocation mechanism, and monitoring, delivery and exit provisions are set out for review and discussion. Modification of the Post-Conflict Country Facility would be included.

2. A limited pool of additional resources to allow the Bank to provide supplementary targeted support for capacity building, knowledge management, etc. in the full range of fragile countries.

These proposals are scheduled to be discussed by the Board at an Informal Meeting scheduled for end-May, and by the ADF Deputies during the next ADF-11 consultation in June. Management would deliver a fully developed proposal for Board consideration by October 2007.

TABLE OF CONTENTS

ENHANCED ENGAGEMENT IN FRAGILE STATES, REVISED APPROACH

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1. INTRODUCTION

1.1 This paper sets out a proposed revised framework to enhance the Bank's operational engagement in circumstances that are characterized as fragile. The case for an enhanced approach, allowing for an increased and more differentiated engagement, has become clear. This is perhaps nowhere more pressing than in Africa, the continent with the highest number of fragile states. The background is essentially two-fold, the Bank has to stay engaged in all its member countries in all types of fragile situations, and the Bank needs to enhance its engagement in particular in countries coming out of conflict and crisis. The latter is especially important given the marked progress that has been made in recent years in resolving many long-running and debilitating conflicts and bringing prolonged political crises to an end. The possibility of successful turnaround is clearly demonstrated by the experience of such countries as Mozambique and Rwanda, where strong country commitment combined with enhanced and more predictable support from development partners, sustained and accelerated the transition out of fragility. Building on the lessons of the past in order to craft more effective engagement for the future is thus particularly urgent for the African Development Bank.

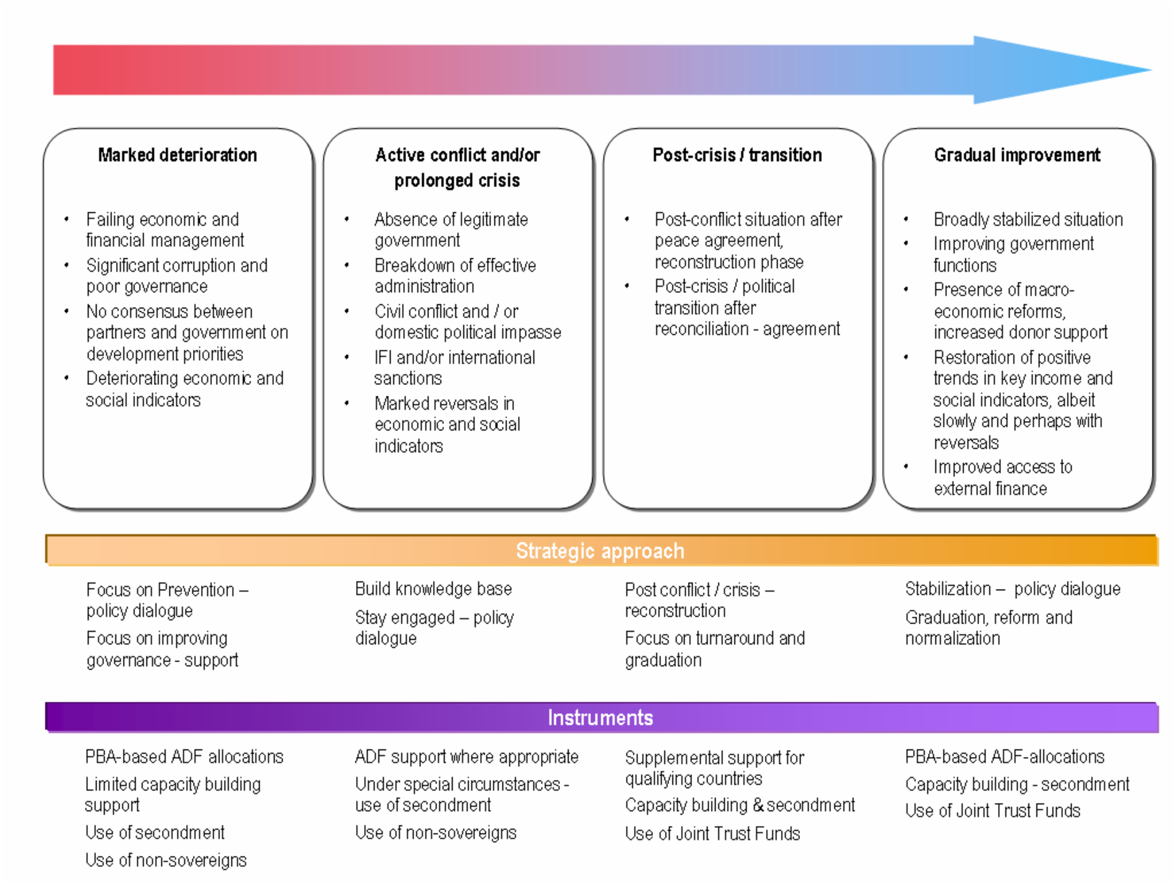
1.2 The current paper incorporates guidance received from the Board of Directors and the ADF Deputies on two earlier drafts, and provides additional clarity and detail on specific issues that have been raised. It is organized as follows: Section 2 presents a summary of the diverse circumstances that broadly characterize pre- and post-crisis situations; Section 3 reviews specific proposals for deeper Bank engagement in a sub-set of these countries; Section 4 discusses specific additional proposals for enhanced engagement across the full spectrum of fragile states; Section 5 identifies proposed changes in the Bank's operational approach needed to ensure more effective delivery of these operations; and, Section 6 reviews options for financing mechanisms.

2. STATE FRAGILITY EXISTS ACROSS A WIDE CONTINUUM

2.1 Fragile circumstances take different forms in different countries and in the same country at different times. Major differences exist in political and public security environments, institutional capacity and performance, government accountability, and commitment to progress along a credible reform path. These differences have major implications for the scope and nature of engagement by development partners. Experience has shown that a uniform approach to widely differing circumstances on the ground has often failed to produce the desired results, and in many circumstances has precluded forms of selective engagement that could be both justified and effective.

2.2 The figure below presents a stylized categorization of these different circumstances. It illustrates a simplified continuum along which circumstances of fragility typically fall – ranging from marked deterioration, to active conflict and / or prolonged crisis, to post-crisis and transition, and finally to gradual improvement. It also sets out, again in very broad terms, possible avenues through which the Bank might become more effectively engaged on a selective and tailored basis. In situations of markedly deteriorating performance, for example, intensified efforts to support government accountability and transparency may contribute to improved capacity. In situations of active conflict, viable options are few, but they could include more intensive engagement with non-sovereign actors and selective capacity support. States that have clearly emerged from conflict and / or prolonged crisis, by contrast, present a strong case for significantly deeper engagement, including through expanded direct investments. And finally, states that have moved into a stage of gradual improvement can accelerate positive trends through targeted institution and capacity-building support.

Figure I: The Continuum Approach



2.3 Movement along this continuum is in reality neither automatic nor unidirectional, as countries may move back and forth between various fragile situations. The goal, however, is to help prevent countries at risk from slippage and to assist countries in post-conflict and post-crisis situations to move forward towards more stable political and economic development. Helping countries progress along the continuum requires an internationally-coordinated strategic effort, covering a country's political, security and socio-economic domains, the latter being the role of the multilateral development banks and the ADB.

2.4 In this regard a differentiated and flexible response is a key. The bulk of resources and efforts under this initiative will be provided to a smaller subset of fragile states, post conflict and post crisis/transition-countries (in this paper called post crises-countries), where the potential for turnaround is present. However, the Bank will stay engaged in countries in all phases of fragility, providing limited assistance to help prevent deterioration, ensuring knowledge building and minimal engagement during crisis and conflict, engaging more deeply and actively in countries transiting out of conflict and crisis, and helping to anchor reforms in countries that are under gradual improvement.

3. POST-CRISIS/TRANSITION SITUATIONS: SPECIAL CHALLENGES AND OPPORTUNITIES

3.1 The primary focus of the proposed initiative is on circumstances characterized above as "post-crisis / transition"[1]. Previous papers have laid out in some detail the particular challenges faced by post-crisis countries working toward successful transition to sustained growth and development, and the major limitations in the Bank's potential support given its current approach and instruments. At the country level, and in brief, they are:

- These countries typically have severely degraded institutional and administrative capacity; physical infrastructure is badly deteriorated or non-functioning; and social services are minimal or non-existent in many areas.
- Economic activity has contracted substantially, with per capita GDP well below pre-crisis levels in real terms; human development indicators (UNHDI) have typically dropped to the lowest quintile.
- Even under optimistic projections available domestic resources are only a fraction of the estimated new investment needed to restore or attain provision of basic services.
- Negative regional spill-over effects are often large, with traditional commercial links severed or badly disrupted.
- Dependency on external assistance tends to be heavy, but access to adequate external resources on appropriate terms is still quite limited relative to needs. Aid flows tend to be highly variable and in many cases have been interrupted for lengthy periods. Absorptive capacity may be a challenge.

3.2 Limitations to effective engagement by the multilateral development banks, including the ADB, are:

- Resources allocated under current performance-based systems tend to be below average by most measures, and certainly low relative to needs and legitimate demands.
- The CPIA assessments on which allocations are largely based capture the very performance deficiencies that result from crisis-driven institutional failure and that require targeted external support. The intended performance focus of the existing PBA mechanism in effect results in low-capacity post-crisis countries competing for limited resources with countries in a sharply different set of circumstances. Moreover, because CPIA ratings are retrospective, by design and due to data constraints, they may not adequately capture evidence that a country is working to "turn the corner."
- Annual allocations provide, as intended, a regular vehicle for performance assessment; however, they also bring considerable uncertainty to the medium-term budget planning process needed for a well prioritized multi-year recovery and reconstruction effort.
- Arrears to the institutions are typically large relative to prospective new flows, and often of long-standing; negotiating a multilateral arrears clearance deal invariably takes considerable time.
- Field presence is at best limited, and often lacking entirely.
- Prolonged crisis invariably undermines the knowledge base of the international institutions, making their own reengagement point one of considerable uncertainty.

[1] The "post crisis-countries" in this paper covers countries characterized by OECD/DAC as in post conflict / crises or political transition situations. Other OECD/DAC categories are: deteriorating governance environments, gradual improvement, and prolonged crisis and impasse. OECD: DCD/DAC (2006)62

- Standard operational systems and methods can result in substantial delays in delivering assistance, and may not adequately monitor either its quality or effectiveness.

3.3 Previous papers also set out a number of basic “Principles of Good International Engagement” in fragile states for institutions such as the ADB that have emerged from extensive work conducted under the auspices of the OECD/DAC. These are summarized in Annex I.

Proposed Framework for Effective Engagement

3.4 The Bank’s proposed operational framework is intended to incorporate, and build out from, these difficult challenges and accumulated experiences. Its core components are:

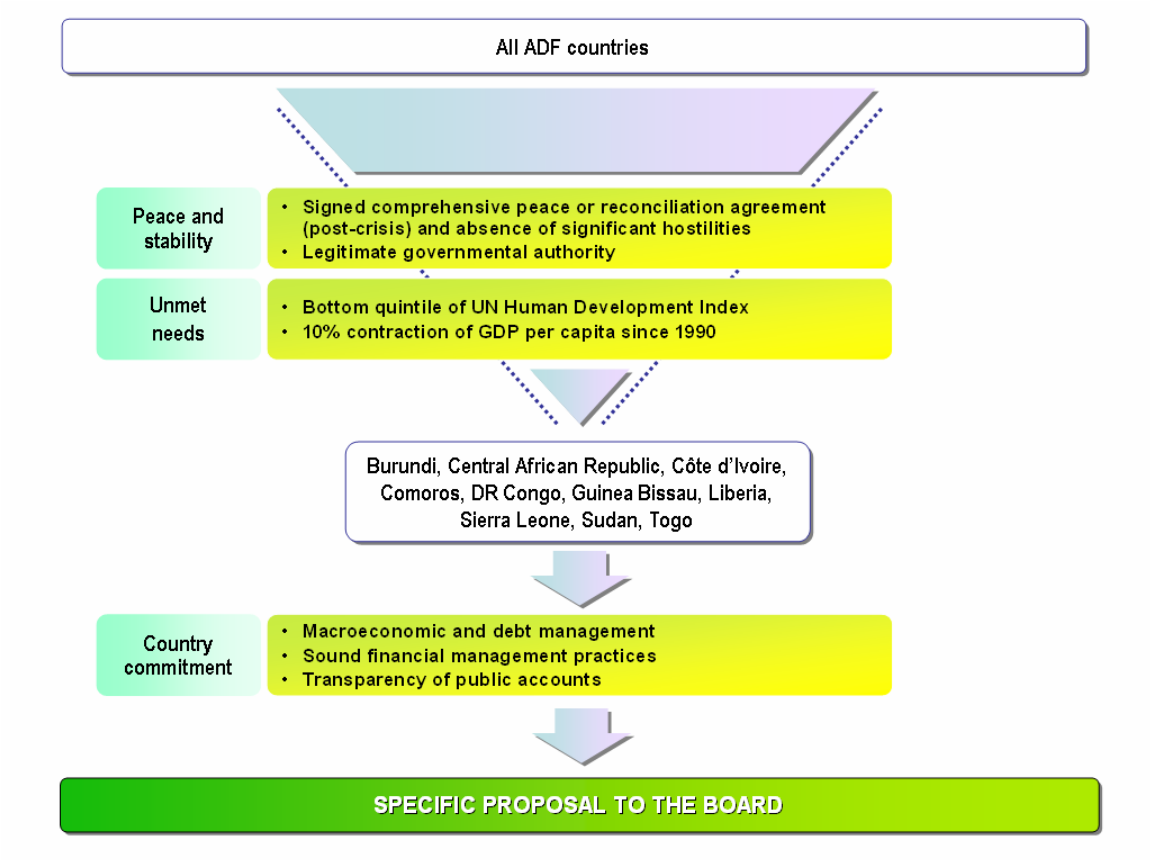
- Engagement triggered by a limited number of threshold indicators that demonstrate clear commitment to transition to social stability, reconstruction and renewed development.
- Provision of supplementary resources (i.e., beyond the calculated ADF performance-based allocation), primarily for priority infrastructure investments and capacity building.
- Supplementary funding committed up-front for three years, and on grant terms.
- Funds specifically dedicated for this purpose from the Bank’s ADF-11 pool.
- Effective collaboration with partners, including joint engagement wherever possible.
- Potential support for up to 2 ADF cycles, with exit expected after no more than 6 years.
- Reduction of delivery bottlenecks, and effective monitoring and reporting.

Filtering Indicators

3.5 The following indicators have been developed to capture selected circumstances that appear to demonstrate a clear commitment to peace and social stability, and compelling economic and social need. We would propose to use these as the basic threshold indicators for potential eligibility of post-crisis/transition countries for supplementary resources.

- An internationally-recognized comprehensive peace agreement or post-crisis or reconciliation agreement has been signed and is in place,
- A functioning governmental authority or transitional government broadly acceptable to stakeholders and the international community is in place,
- There are no ongoing hostilities of any significance,
- The country is in the bottom quintile of the UN Human Development Index, and
- Per capita GDP has contracted by more than 10% in real terms since 1990.

3.6 Internal assessment has identified a preliminary indicative list of 10 countries potentially meeting these circumstances, albeit still with wide variety (see Figure 2 below). Specific recommendations as to eligibility for individual countries would be considered against these indicators, and on the basis of deeper analysis. Moving ahead with a supplementary program would require in addition commitment to a satisfactory macroeconomic framework, sound financial management practices and transparency of the public finances (including with respect to debt). A determination of these conditions would result from dialogue with the country itself and consultations with the World Bank and other partners. Any specific proposal for ADB engagement via supplementary funding would be submitted to the Board for approval on a case-by-case basis.



Resource Allocation

3.7 Any proposed resource allocation mechanism should satisfy several basic criteria:

- It should provide a level of supplementary resources, incremental to existing flows, sufficient to materially expand the available pool of resources and Bank operations in support of recovery and transition.
- The amount of resources should be appropriately scaled relative to the size of the economy and its development circumstances.
- Resource levels should be determined through a transparent and predictable process, and seen as equitable relative to resources similarly provided to other recipients.
- Resources should be available with high certainty for a multi-year period.
- Individual allocations from what will likely be a fixed, limited pool should not excessively reduce the capacity of the pool to meet the needs of other eligible countries.

3.8 Against these criteria we propose the following approach to determine country allocations.

- Set as a baseline, or "anchor," the average of the two highest calculated ADF-10 allocations, minus any PCEF enhancement[2]. These allocations: a) capture the relative size and economic development differences between individual countries; b) reflect the best available recent measures of performance, through the CPIA; and, c) do not reflect any prior judgment about post-conflict or post-crisis funding needs.

- The supplementary amount to be provided would be set at double this baseline allocation. Thus, a country whose average "high 2" allocation during ADF-10 was UA10M (for 3 years) would be eligible for supplementary funding of UA20M (for 3 years).

- The basic performance-driven allocation would continue to be made during ADF-11, in addition to any supplementary allocation. Thus, a country whose ADF-10 allocation was as above, and whose ADF-11 allocation (for 3 years) is UA15M, would have a total pool of available resources of UA35M over the three year period.

3.9 Given the wide range in size of potentially eligible countries, a large country could potentially receive under this approach a supplementary allocation that is very large in absolute volume terms. With the competing demands for and constraints upon the overall ADF-11 pool from which these supplementary funds would be constituted, there is a real risk that large-country allocations would crowd-out resource availability for smaller eligible countries. Similarly, some minimal level of supplementary funding would be necessary to ensure meaningful additionality.

- A minimum supplementary allocation of UA10M and a maximum of UA60M are proposed.

3.10 Annex II sets out the potential supplementary allocations under this scenario for the 10 countries identified above. It also presents two alternative illustrative scenarios: supplementary allocations set at 1.5 times the ADF-10 baseline allocation; and, supplementary allocations set at 2.5 times the ADF-10 baseline allocation. The central scenario would require supplementary resources of approximately UA350M for this subset of countries for the ADF-11 period.

Monitoring and Exit

3.11 As noted above, the base period for enhanced support is proposed to be 3 years. Continuation of support after the first 3-year period would require (in addition to funding availability under ADF-12) a determination of adequate performance during the first cycle and explicit Board approval on a case-by-case basis.

3.12 The end-of-cycle assessment would focus on achievements with respect to commitments and benchmarks agreed at the entry point, and set out in the country's programming document. Performance benchmarks will inevitably vary across countries, but are expected to include economic governance, especially in strengthening public financial management, and appropriate contracting and management of external debt. The ADF-11 PBA process would also contribute an ongoing performance assessment that would feed into this end-of-cycle assessment. Performance with respect to programs supported by other partners would be reviewed. All of this would factor into a Management proposal to the Board to extend supplementary assistance for an additional three years.

3.13 While the basic presumption would be assured supplementary funding for a full three year period, a significant departure from the agreed basis for supplementary support -

[2] Under the ADF mechanism, an annual PBA calculation is made to determine the ADF allocation envelope for the full 3-year ADF cycle. The calculated envelope will, of course, change to reflect changes in the annual performance assessment

- such as a breakdown in agreed political arrangements or public security, or accumulation of new debt on inappropriate terms -- would trigger a rapid review that could result in premature exit from the supplementary program. Any such decision would be submitted to the Board for review and approval.

3.14 This proposal, together with its preliminary estimates of required financing (largely for supplementary ADF allocations), is based on an indicative list of countries potentially eligible at this time. However, we must also anticipate that eligible circumstances may also develop in additional countries as a result of their moving into post-crisis/transition status. In such cases where comparable access to supplementary resources is justified, Bank Management would bring specific proposals to the Board for review and approval. Such proposals would also need to include a clear identification of the supplementary financial resources to be mobilized, and their source.

4. ENHANCED ENGAGEMENT IN OTHER FRAGILE SITUATIONS

4.1 The specific proposals outlined above have focused on the sub-set of post-crisis and transition countries meeting established threshold criteria. These countries also have more absorptive capacity than other fragile states. However, as indicated earlier (including in Figure 1), the Bank has a role to play also in other fragile situations, in some cases with important contributions. In the latter case, enhanced engagement by the Bank will be on a targeted and selective basis. In particular, intensified provision of policy advice and efforts to strengthen institutional and administrative capacity could contribute materially to stabilizing deteriorating situations, to promote a successful exit from active crisis, and to accelerate the rate of improvement that may already be underway. Targeted interventions aiming at anchoring reforms and improving performance in these cases can make an important contribution to effective use of ADF-resources accessed on a normal PBA-basis.

4.2 Specifically, the Bank should have a pool of dedicated supplementary resources available to provide incremental (i.e., beyond current levels) support for capacity-building, such as through secondments, knowledge building, and targeted interventions channeled through non-sovereign entities (such as international procurement or auditing firms) that may have unique capacities to engage effectively. Secondment of seasoned professionals would help fill critical gaps at the senior executive level, building leadership capacity on a targeted basis and helping to develop senior civil servant capacity in management and implementation of reforms both in post-crisis countries and other fragile states.

4.3 This program would be financed from the supplementary facility proposed below, would consist mainly of small grants, and would be additional to a country's regular ADF allocation. Overall financing requirements for these expenditures are tentatively estimated to be in the range of UA 35 million, equivalent to 10% of the proposed core supplementary resources for post-crisis/transition countries under the scenario outlined above. Proposals would be based on short Country Briefs or Country Dialogue Papers and submitted to the Board on a case-by-case basis.

5. IMPROVING DELIVERY

5.1 If the Bank is to provide more timely and effective support in especially challenging circumstances it will need to address a number of current operational constraints. Some important steps are already underway Bank-wide as part of the ongoing institutional reforms and are expected to produce clear positive change. However, there is also a need for additional measures in order to ensure that the supplementary initiative proposed here achieves maximum impact with minimal delay.

5.2 Measures already in process to improve the Bank's delivery performance include:

- Significant streamlining of business processes, particularly with respect to the project development and review process, that will sharply reduce internal processing delays and improve focus, quality at entry, and performance monitorability.
- We will shortly bring the Board proposed revisions to current Eligible Expenditure Guidelines that will allow for up to 100% Bank financing, including for recurrent expenditures, taxes, and local costs.
- Country Strategy papers are being restructured to sharpen their focus on results and specific priorities, and to allow the more flexible treatment that different country circumstances and Bank strategies require.
- Country teams are now central to strategy development and operational delivery, and explicitly accountable for effective results on the ground. Significantly more Bank staff are now on the front line of operations.
- We are working actively to fill current vacancies in the Operations Departments and expect to have a full complement by the end of the year.
- Field Offices have been opened in a number of the specific countries identified above, with staff skills tailored to ensure capacity in country-specific priority areas. In addition, capacity can be deployed on a regional basis from existing field offices.
- Decision authority is being delegated downward and outward to the field offices; reduced delays and greater staff level initiative in solving problems are expected.
- A restructured Procurement and Financial Management Unit will have increased skills, staffing and accountability, particularly in financial management. Revised internal procedures will substantially improve oversight and quality control, and ensure that unnecessary and unreasonable delays are eliminated.
- The Bank's Partnership Unit is being invigorated to improve the quality of relationships with external partners, build innovative new partnerships, and ensure more effective use of the special purpose resources entrusted to us.

5.3 Beyond these steps, which promise to improve operational performance Bank-wide, we are proceeding with the following additional initiatives specific to improving results and performance under a supplementary funding program:

- A Focal Point for Fragile States has been established, with dedicated staff.
- The Operations Committee would meet quarterly specifically to assess Bank operations in countries receiving supplementary funds.
- A series of specific rapid-response procedures to speed up disbursement and procurement activities, as set out in Annex III, would be utilized on the basis of case-by-case approval by the Board[3].
- All procurement and disbursement activities in recipient countries would be explicitly benchmarked and monitored to eliminate unnecessary delays.
- The Bank's decentralization process is being kept under review and an expanded field presence in some of these countries may be proposed.
- Potential budget implications for delivering supplementary assistance as outlined will be explicitly considered as part of the 2008 budget cycle.

5.4 There are additional possible steps in a number of areas that would require fuller examination and discussion with the Board.

- The threshold for grants in the area of capacity-building should be raised above the current range of 20 - 50 %, to be implemented on a case-by-case basis.

[3] The template of rapid response-procedures is building on the new procedures approved by the World Bank: "*Strengthening the World Bank's Rapid Response and Long-Term Engagement in Fragile States*" and "*Toward a New Framework for Rapid Response to Crises and Emergencies*", both January 12, 2007.

- Subject to agreement if its sponsors, unutilized resources in the Project Preparation Facility should be reprogrammed to assist in delivery of supplementary operations.
- Bank participation in joint trust fund financing, such as through Multi-Donor Trust Funds (MDTF) involving pooling of funds by partners, would provide an important new avenue for partnership in fragile situations. New guidelines would be required.
- The complex legal issues around channeling resources through non-sovereigns are now under review by the General Counsel. This work will proceed on an accelerated basis and is expected to produce some specific proposals.

5.5 Other issues that have been raised by the Board will be addressed in more detail in the full Board paper in the fall. They include:

- International Coordination with international partners within a peace building framework at the country level, and follow up on the recommendations of the MDB Working Group on fragile states.
- Areas of engagement: choice of areas of focus, cross-cutting issues, addressing the regional dimension of state fragility, the spill-over effects, the challenge of resource rich fragile states and corruption
- Implementation-arrangements: programming and operational instruments and processes (e.g. Country Briefs, the secondment modality, use of Joint Trust Funds and non-sovereigns, field-presence, human resources & Bank-capacity, and estimated budget implications).

5.6 In aggregate, the Bank-wide steps already underway coupled with specific additional initiatives would substantially improve our capacity to deliver and effectively monitor an intensified operational program in selected countries.

6. FINANCING MECHANISM

6.1 Effective implementation of the proposed revised approach will require additional resources on a substantial scale and a dedicated mechanism to deliver them for the intended purpose. This section summarizes the major financial components of the approach presented, and identifies and reviews possible options.

6.2 The proposals above comprise three discrete but closely linked funding components amounting to UA 400 M in aggregate (this would be in addition to whatever ADF-11 allocation is made for the countries out of the basic PBA pool).

- An estimated UA 330 M required for supplementary operational support in post-crisis/transition countries.
- An estimated UA 33 M (or 10% of the above amount) to finance selective additional capacity building activities in other fragile countries.
- An estimated UA 36 M to bring PCCF funding to a level that would allow it to support arrears clearance in three additional (post-crisis/transition) countries.

6.3 There are prospectively three sources of funding: new ADF-11 resources; direct contributions from ADF donors beyond basic ADF-11 commitments; and, direct contributions from non-traditional sources, possibly including non-members.

6.4 The financing vehicle to receive these funds which are intended to be supplemental to the PBA-driven resource pool should ideally be structured to: enable up-front commitments for initially identified countries and purposes; provide the funding certainty needed for multi-year commitments; be accessible to supplementary voluntary contributions from individual supporters; be easily re-fundable for a second ADF cycle, if justified; and, be fully transparent. We have identified a modified set of options that could be considered.

6.5 One option originally presented by Bank Management was to increase allocations to eligible countries by modifying the basic CPIA mechanism to better capture specific aspects of fragility. We have not considered this option further for several reasons: it would further complicate the PBA process; supplementary resources for eligible countries would come at the expense of non-eligible countries which may be strong performers; experience with ADF-10's "Post–Conflict Enhancement Factor" has been mixed, and it has not provided recipients with significantly expanded resources; the overall transparency and perceived equity of the PBA process would probably be reduced; and, it would by definition be closed to the possibility of additional voluntary contributions from individual supporters.

6.6 Specific financing options that could be considered are as follows:

- ***<u>Option 1</u>: Create a separate earmark or set-aside within ADF-11.***

  This approach would set a clear and transparent amount of ADF resources to supplement basic allocations through the Bank's regular PBA system. It would simplify and strengthen the transparency of the PBA system by removing the PCEF. It would require a special purpose allocation mechanism (such as discussed above) operated alongside the normal PBA. However, it would also be funded exclusively by ADF resources; any prospective voluntary contributors would require new, separate funding arrangements.

- ***<u>Option 2</u>: Create a new special purpose ADF window.***

  This option would also enhance the PBA system for regular ADF resources by eliminating the added complexity of the PCEF. It would create an assured pool of resources to fund this initiative on the basis of clear and transparent criteria and estimates. The key difference is that a separately constituted new window or fund would be able to receive voluntary contributions from donors, including non-ADF members, while being administered by the Bank. It would be easier to introduce adjustments to the Bank's operational guidelines for use of such resources – such as direct funding to non-sovereigns—than to revise the Bank's general rules. With this structure allocations could in principle be made prior to arrears clearance. However, potentially difficult decision-making and governance issues could arise and would need to be resolved as well as challenges related to ADF burden-sharing formulas.

In both of the above cases Deputies would be separately requested to amend the Post-Conflict Country Facility (PCCF). The PCCF was initially funded as part of ADF-10 on the basis of a specific list of countries expected to qualify over the course of the replenishment cycle. The PCCF has functioned largely as intended and remains broadly on track to finance arrears clearance programs for each of these countries as circumstances demand. However, the indicative list of countries potentially eligible for the new facility proposed here included three additional countries for which PCCF-style treatment would be required. The estimated incremental financing need for PCCF is UA 36M. A third option would therefore be to combine the supplementary fund and the re-funding of the PCCF.

- ***<u>Option 3</u>: New Fragile States Facility.***

  Option 3 would combine the modification and re-funding of the PCCF with the Option 2 proposal to create a separate ADF fund. It would include all of the advantages of Option 2, and in addition create a single facility with the resources and instruments to deal effectively with the full range of the Bank prospective supplementary fragile state engagements – arrears clearance; selective support for capacity building; and, additional ADF allocations. The benefits would be greater ease of administration, more effective oversight and coordination, and a more seamless sourcing of services and support.

	Pros	Cons
Option 1: ADF-11 earmark or set aside for eligible countries.	• Simplifies PBA by removing PCEF, but otherwise leaves the PBA unaffected. • Sets clear and transparent amounts for eligible countries. • Easily re-fundable under ADF-12.	• Needs separate allocation system • Multiple ADF windows add some administrative complexity. • Relies exclusively on ADF resources. • Voluntary contributions would need to be negotiated and constituted separately
Option 2: Separate window or Fund parallel to ADF-11	• Simplifies PBA as noted above. • Open to voluntary contributions. • Greater flexibility on new processes and guidelines. • More easily harmonized with other funding sources. • Integrated administration of funds from multiple sources. • Sets clear and transparent amounts for eligible countries.	• Needs separate allocation system. • Potential governance complexities from burden-sharing concerns or non-ADF contributors. • Incremental administration burden, in addition to ADF.
Option 3: Combined PCCF and Supplementary Pool into a Single Facility	• Same as Option 2 above. • Single operational vehicle for full range of activities.	• Same as Option 2 above.

6.7 On balance, Management sees Option 3 as the preferred mechanism. It would better facilitate mobilization, management and pooling of resources from the full range of potential sources, provide the greatest flexibility for operational engagement in fragile situations, including through integrated multi-donor programs, and provide greater transparency through a single consolidated account.

7. CONCLUSIONS

7.1 This paper has outlined a proposed revised operational framework, through which the Bank could enhance its engagement and development effectiveness in fragile regional member states. It has presented a set of initiatives that would position the Bank to engage more effectively across the fully range of fragile states in Africa, and particularly in countries in the post-crisis/transition phase where greater support is especially critical. Specific proposals are made with respect to country eligibility, resource allocation, operational priorities, implementation and delivery requirements, and financing options.

7.2 These proposals will be presented to the Board in an Informal Board meeting scheduled for 31 May 2007. Deputies' views are requested during the 11 June 2007 ADF-11 consultation in Tunis.

7.3 Based on recommendations, comments and observations received during these two consultations, Management will finalize a proposed strategy for Board consideration in the fall of 2007.

Annex I

Principles and Themes Underpinning Effectiveness in Fragile States

i) **Prevention is better than cure** – Working to prevent states from falling into fragility or preventing fragile states from collapsing is better, and has a higher pay-off, than marshalling support to rebuild them afterwards.

ii) **Enhancing Country Ownership** - By ensuring that fragile states own and are in the driver's seat in implementing programs and projects for turning-around their countries.

iii) **Focus on State-Building as the Central Objective:** States are fragile when their structures collapse or lack the political will and/or capacity to provide the basic functions needed for poverty reduction, development and to safeguard the security and human rights of their population.

iv) **Focusing on selectivity and value added on the part of the Bank** – The role of the Bank is to add value to the efforts of other international development partners.

v) **Establishing Strategic Frameworks and Coordination** – Multi-dimensional nature of state fragility – encompassing peace, security, economic and administrative domains –implies that no single donor can or will be able to address all the development challenges in fragile states.

vi) **Speedy Response and Adaptability** – Fragile states require urgent response as situations are fluid and change very rapidly.

vii) **Prioritization and Sequencing of interventions** – In complex fragile states environments, where virtually every sector requires reforms, appropriate sequencing of reforms is crucial for achieving intended outcomes.

viii) **Long-term and sustained engagement** - Solid turnaround in political and economic environments in fragile states and situations in Africa is not likely to take place within the short run.

ix) **Regional Dimensions of State fragility** – Strategy should take into account the regional dimension of state fragility, primarily because of huge spill-over effects that fragile states generate to their neighboring countries and sub-regions.

Annex II

Illustrative Supplemental Fund Allocations

Country	GNI/pc	Pop (million)	2006 ADF10 alloc. w/o PCEF	TOP-UP OPTIONS* Option 1 1.5x ADF10	TOP-UP OPTIONS* Option 2 2x ADF10	TOP-UP OPTIONS* Option 3 2.5x ADF10	TOTAL ALLOCATION** Option 1 1.5x ADF10	TOTAL ALLOCATION** Option 2 2x ADF10	TOTAL ALLOCATION** Option 3 2.5x ADF10
Burundi	90	7.21	26.55	39.83	53.11	66.39	66.39	79.66	92.94
CAR	260	3.88	8.82	13.23	17.64	22.05	22.05	26.46	30.87
Comoros	450	0.60	5.29	7.93	10.57	13.22	13.22	15.86	18.50
Congo DRC	100	53.15	216.95	60.00	60.00	60.00	276.95	276.95	276.95
Cote D'Ivoire	660	16.84	17.22	25.84	34.45	43.06	43.06	51.67	60.28
Guinea Bissau	140	1.49	7.22	10.83	14.44	18.05	18.05	21.66	25.27
Liberia	110	3.37	8.61	12.92	17.23	21.54	21.54	25.84	30.15
Sierra Leone	150	5.34	22.06	33.09	44.12	55.15	55.15	66.18	77.21
Sudan	460	33.55	39.27	58.91	60.00	60.00	98.18	99.27	99.27
Togo	310	4.86	10.54	15.81	21.08	26.35	26.35	31.62	36.89
Total PBA allocation from regular ADF pool			362.54						
Topping Up amount for Fragile States Fund (FSF)				278.38	332.64	385.80			
Total allocation (assuming ADF-10 level)							640.93	695.18	748.34

Note
* All topup amounts based on ADF-10 2006 allocated amount minus the PCEF. ADF-10 allocations are for the full 3-year cycle. We asume a cap of 60M for DRC
** Assuming 2006 allocation plus top-up amount

<u>Rapid Response Procedures: Possible Template for Topping Up - Countries</u>

The Rapid response-procedures would be applied to the topping-up countries only, and be subject to ex-ante approval by the Board on a case by case basis.

To ensure the Bank's ability to speed up ***disbursement,*** it could:

- provide for a quick-disbursing component designed to finance (or re-finance) a positive list of goods that have been identified as necessary

- enable the Vice President concerned to approve a temporary increase in the cost-sharing limits in all Bank-financed operations in such country if so requested by the borrower.

- permit the Bank to finance up to 100 percent of the expenditures needed to meet the development objectives, including recurrent expenditures, local costs, and taxes;

In Procurement, a more rapid response could include:[1]

- the use of rapid procurement methods (direct contracting or simple shopping) for the procurement of services of qualified UN agencies/programs and/or suppliers (for goods) and civil works contractors already mobilized and working in emergency areas (for works);

- use of third party, independent procurement agencies;

- sole sourcing of consulting firms already working in the area and which have a proven track record for the provision of technical assistance;

- extension of contracts issued under existing projects for similar activities through increase in their corresponding contract amounts;

- where alternative arrangements are not available, the use of Force Account for delivery of services directly related to the emergency; and

- the use of NCB, accelerated bidding and streamlined procedures and application of provisions on elimination, as necessary, of bid securities.

<u>Ex-post controls:</u> The risks associated with the need for much greater speed early on, such as listed above, will be balanced by more careful and intensified supervision later in the operation, including additional *ex post* reviews, audits by international firms and other measures, and application of appropriate remedies. There will be regular reporting to the Board in this regard.